TAN KAH HOE & ANOR

v.

BUDAYA ADIL SDN BHD

HIGH COURT MALAYA, KUALA LUMPUR
STEVE SHIM J
[COMPANIES WINDING UP NO: D5-28-40-1998]
3 SEPTEMBER 1999

COMPANY LAW: *Winding-up - Disposition of property - Subsequent to presentation of petition - Disposition sought to pay off legal fees - Whether court should validate disposition - Considerations - Bona fides of disposition - Pari passu principle - Whether disposition would confer advantage to one creditor over other creditors - Whether solicitors had prior knowledge of presentation of petition - Companies Act 1965, s. 223*

This was the respondent company's application under s. 223 of the Companies Act 1965 ('the Act') for RM60,000 to be paid out of its frozen current account to its solicitors ('M/s RDL') to offset any legal fees that might be due to M/s RDL in respect of (i) resisting the instant winding-up petition filed by the petitioners and (ii) prosecuting an action brought by the respondent against its previous directors.

Held:

[1] M/s RDL was aware of the winding-up petition when it agreed to represent the respondent in the proceedings. It also appeared that the disposition had not crystallised at the time of the application, thus raising serious doubts as to the *bona fides* of the disposition.

[2] If the disposition was validated, M/s RDL would, as a creditor, be paid in full, and this would mean that it had secured an advantage over all the other creditors in contravention of the *pari passu* principle.

[3] The respondent's assertion that the action against its previous directors would benefit all its creditors presupposed the very success of the action. If the action were to fail, the respondent would even incur additional legal expenses.

[4] The power of the court to validate the disposition of a company's property under s. 223 of the Act is governed by the general principles applicable to judicial discretion.

[Application dismissed.]

Case(s) referred to:

Bianco Hiring Services Pty Ltd v. Adelaide Truss & Frame Pty Ltd [1992-1993] ***(refd)***

BSN Commercial Bank (M) Bhd v. River View Properties Sdn Bhd [1996] 1 BLJ 307 ***(refd)***

Kimoyama Electrik (M) Sdn Bhd v. Metrobilt Construction Sdn Bhd [1990] 2 CLJ 795 ***(foll)***

Prospect Electricity v. Advanced Glass Technologies of Australia Pty Ltd [1996] 14 CLA CLR 1721 ***(refd)***

Re AI Levy (Holdings) Ltd [1963] 2 All ER 76 ***(refd)***

Re Wiltshire Iron Company, ex p Pearson [1867-1868] 3 Ch 443 ***(refd)***

Tellsa Furniture Pty Ltd v. Glendare Nominees Pty Ltd [1987] 5 ACLC 662 ***(refd)***

Legislation referred to:

Companies Act 1965, s. 223

Companies Act 1862 [UK], s. 153

Companies Act 1948 [UK], s. 227

Companies Code [S Aust], s. 368

For the petitioners - CC Chan; M/s Skrine & Co

For the respondent - SY Ng (YM Raja Eileen Soraya with him); M/s Raja, Darryl & Loh

Reported by Alex KC Lee

JUDGMENT

Steve Shim J:

This is the respondent's application by way of notice of motion at encl. 42 made pursuant to s. 223 of the Companies Act 1965. Prayer (1) states:

> (1) that leave be granted for the sum of RM60,000.00 to be paid out of the Respondent's current account no. 004012-618950 held at Maybank, No. 171-175, Jalan Munshi Abdullah, 75100 Melaka, to the Respondent's solicitors, Messrs. Raja Darryl & Loh, to be held in the Respondent's client's account and to be utilized by Messrs. Raja Darryl & Loh towards off-setting any sums or any part thereof due to Messrs. Raja, Darryl & Loh under any invoice which will be rendered to the Respondent from time to time in respect of and arising out of the proceedings herein and the proceedings brought by the Respondent against its previous directors.

The application is supported by the affidavit of Ong Chen Peng, a shareholder and managing director of the respondent affirmed on 19 March 1999. The petitioners have opposed the application filing a notice of intention to use two affidavits in reply affirmed by them on 29 May 1998 and 6 November 1998 respectively.

The factual background to the application can be briefly stated herein. By a letter dated 23 March 1998, the respondent received a letter from Maybank, Jalan Munshi Abdullah, Melaka branch (the bank) informing that the bank had frozen the respondent's current account, apparently as a result of having notice of the winding up proceedings before the court. The respondent is presently involved in two litigations, one relating to disputing the winding-up petition lodged by the petitioners and the other concerns the respondent's action against the 1st petitioner and one Wong Kim Yong for, amongst other things, misappropriation of assets. The respondent has engaged M/s Raja Darryl & Loh to handle both these litigations. Hence, the notice of motion at encl. 42.

It is the respondent's case that a sum of RM60,000, which it is presently seeking leave of the court to utilise, is for the sole purpose of paying its legal fees that have arisen and will be incurred due to those proceedings and that the orders sought are necessary to enable the respondent to obtain professional assistance to resist the winding-up petition filed by the petitioners and, at the same time, to commence legal action against the 1st petitioner and another.

Now, s. 223 of the Companies Act 1965 stipulates:

> Any disposition of the property of the company including things in action and any transfer of shares or alteration in the status of the members of the company made after the commencement of the winding-up by the court shall unless the court otherwise orders be void.

In *Re Wiltshire Iron Company, ex p Pearson* [1867-1868] 3 Ch 443, Lord Cairns, LJ in explaining the scope of s. 153 of the English Companies Act 1862 (which is in *pari materia* to our s. 223) had this to say:

> The 153rd section no doubt provides that all dispositions of the property and effects of the company made between the commencement of the winding-up (that is the presentation of the Petition) and the order for the winding-up, shall, unless the court otherwise orders, be void. This is a wholesome and necessary provision, to prevent, during the period which must elapse before a Petition can be heard, the improper alienation and dissipation of the property of a company in **extremis.** But where a company actually trading, which it is in the interest of everyone to preserve, and ultimately to sell, as a going concern, is made the object of a winding-up Petition, which may fail or may succeed, if it were to be supposed that transactions in the ordinary course of its current trade, *bona fide* entered into and completed, would be avoided and would not, in the discretion given to the court, be maintained, the result would be that the presentation of a Petition, groundless or well-founded, would, *ipso facto,* paralyse the trade of the company and great injury, without any counter balance of advantage, would be done to those interested in the assets of the company.

Section 153 was subsequently replaced by s. 227 of the English Companies Act 1948, by the time Buckley, J came to consider it in *Re A I Levy (Holdings) Ltd* [1963] 2 All ER 76. His Lordship described s. 227 (which is in *pari materia* to our s. 223) in this way:

> Section 227 of the Companies Act, 1948, has in one form or another formed part of the companies winding-up legislation since it appeared as s. 153 of the Companies Act 1862. I have been referred to various authorities in which the jurisdiction has been either exercised or commented on, the earliest of which is *Re International Life Assurance Society, Gibbs & West's* case, where, Sir R, Malins, V-C cited a passage from Lord Cairns' judgment in *Re Wiltshire Iron Co, Exp Pearson*, which I need not read. That passage indicated a broad view of the nature of the jurisdiction conferred by the section and indicated that it was designed to preserve the value of the assets of a company for the benefit of the people interested in the assets notwithstanding the pendency of the winding-up proceedings, in order that the company might not be unduly hampered in carrying out transactions which might be for the benefit of those interested in the value of its assets.

It is interesting to note that *Re Wiltshire supra* had been cited with approval by the Supreme Court of South Australia in *Bianco Hiring Services Pty Ltd v. Adelaide Truss & Frame Pty Ltd (in liquidation)* [1992-1993]. Thereat Leqoe J took the opportunity to further explain the equivalent s. 368 of the Companies (SA) Code when he said *inter alia*:

> ... the Federal Court pointed out, that what lies behind s. 368 is the prevention of the improper alienation and dissipation of the company's property; it is not intended to reach out to transactions by which a creditor receives assets covered by his security at a time when he was entitled to have them.
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> On the one hand, while the purpose of s. 368 is undoubtedly to minimise hardship to the body of creditors generally, and which hardship to the particular creditor must be taken into account, it can hardly ever be conclusive. It has been held, consistently with the views expressed by Lord Cairns LJ in *Re Wilshire Iron Co, Ex parte Pearson, supra*, that the discretion conferred upon the court by this section to validate transactions, is controlled only by general principles applicable to judicial discretion ... Whether the court validates a disposition of the company's property made after the commencement of a winding-up is a matter for the discretion of the judge; and it has to be determined on the facts of each case by what is just and equitable in all the circumstances, special regard being had to whether the disposition was made *bona fide.*

Quite clearly, s. 223 confers a discretion upon the court in determining, whether or not, having regard to the particular facts and circumstances of a given case, it should validate a disposition of property of a company. The power of the court to do so is controlled by general principles applicable to judicial discretion. The onus is on the applicant to satisfy the court of circumstances which would justify the exercise of the discretion to sanction the disposition.

In the instant case, the sole reason for seeking leave is to allow the respondent to fund the legal costs or fees in first resisting the winding-up petition launched by the petitioner and secondly to prosecute an action against its previous directors for *inter alia* misappropriation of assets. As such, it is contended that the application is purely for the benefit and assistance of the respondent as well as the creditors thereof. The petitioners have of course disputed this. A number of factors require consideration.

First, the facts disclosed in the affidavits seem to indicate that the respondent's solicitors, to whom the RM60,000 were to be disbursed, had full knowledge of the winding-up petition before accepting the contract in respect of the two litigations mentioned above. There is also indication that the disposition had not crystallised at the time of the application. In the circumstances, there is quite evidently serious doubt as to the *bona fide* of the said disposition; (see *BSN Commercial Bank (M) Bhd v. River View Properties Sdn Bhd* [1996] 1 BLJ 307; *Tellsa Furniture Pty Ltd (in liq) v. Glendare Nominees Pty Ltd* [1987] 5 ACLC 662.)

Secondly, again the affidavits would indicate that if leave to validate was granted, it would have the effect of paying the respondent's solicitors, a creditor, in full, thereby securing an advantage over the rest of the creditors. From the facts, it is, I think, sufficiently clear that the disposition was entered for the express purpose of securing an advantage to one creditor over the rest of the creditors. This would be against what was described as the *pari passu* rule in *Prospect Electricity v. Advanced Glass Technologies of Australia Pty Ltd* [1996] 14 CLA CLR 1721. Such a rule was apparently adopted and applied in *Kimoyama Electrik (M) Sdn Bhd v. Metrobilt Construction Sdn Bhd* [1990] 2 CLJ 795; [1990] 3 MLJ 309 wherein Zakaria Yatim J (as he then was) held the view that the court could not exercise its discretion to make a validating order if the result of the order was to make one or more creditors being paid in full.

Thirdly, as I have stated, it is the respondent's stand that the creditors would also benefit if the application is granted because part of the funds would be required to pay for the litigation involving its action against the previous directors for an account of the monies allegedly misappropriated by them. Such a proposition merely presupposes the success of that action. In the absence

of evidence establishing a *prima facie* case, this is nothing but an unreliable speculation or supposition. If the action lodged by the respondent were to fail, the respondent and therefore the creditors would conceivably be saddled with increased legal costs. From the facts as disclosed in the affidavits, I am not satisfied that the other creditors of the respondent would benefit from the application.

From the reasons stated, I do not think it fair and proper to grant the motion in term thereof. Accordingly, I will dismiss it with cost to be taxed unless otherwise agreed.